Report

of the

Examination of

The Northwestern Mutual Life Insurance Company

Milwaukee, Wisconsin

As of December 31, 2002

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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September 11, 2003

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Commissioners:

In accordance with your instructions, a compliance examination has been made of the affairs and financial condition of:

THE NORTHWESTERN MUTUAL LIFE INSURANCE COMPANY
Milwaukee, WI

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of the company was conducted in 1998 as of December 31, 1997. The current examination covered the intervening period ending December 31, 2002, and included a review of such 2003 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations, and included the following areas:

History
Management and Control
Corporate Records
Conflict of Interest
Fidelity Bonds and Other Insurance
Employees' Welfare and Pension Plans
Territory and Plan of Operations
Affiliated Companies
Growth of Company
Reinsurance
Financial Statements
Accounts and Records
Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

Independent Actuary's Review

Independent actuaries were engaged under a contract with the Office of the Commissioner of Insurance. They reviewed the adequacy of aggregate life and accident and health reserves, dividends to policyholders, cash flow testing, deferred and uncollected premiums for life insurance, due and uncollected premiums for health insurance, and in force testing. The results of their work were reported to the examiner-in-charge. As deemed appropriate, reference is made in this report to the actuaries' conclusion.

II. HISTORY AND PLAN OF OPERATION

The Northwestern Mutual Life Insurance Company (NML or "the company") was organized in 1857 as The Mutual Life Insurance Company of the State of Wisconsin. The name was changed in 1865 to the current name.

The company is licensed in all 50 states and the District of Columbia. The percentage of 2002 direct premiums written in various states was as follows:

State	Direct Premium*	% of Total
New York	$ 666,378,257	9%
California	582,050,245	8
Illinois	557,404,568	7
Wisconsin	417,682,240	5
Florida	410,293,126	5
Texas	326,798,313	4
New Jersey	292,293,576	4
Georgia	275,671,691	4
Ohio	261,531,817	4
Connecticut	259,446,657	3
Michigan	259,436,245	3
Pennsylvania	249,939,372	3
Minnesota	243,353,067	3
All others	2,842,451,754	38
Totals	$7,644,730,928	100%

* Premiums are from Schedule T. They include annuity considerations, but do not include dividends applied to purchase paid up additions and other amounts not allocated by state.

The major product marketed by the company is ordinary life insurance written on a participating basis. Other products include individual annuities, disability income insurance, and variable life insurance and variable annuities. In addition, NML offers CompLife, which combines a basic amount of whole life, plus extra protection consisting of one-year term insurance and paid-up additions provided by policy dividends. The major products are marketed through the company's 8,000 career agents.

The following chart is a summary of the net insurance premiums earned by the company in 2002. The growth of the company is discussed in the Financial Data section of this report.

Line of Business	Direct Premium	Reinsurance Ceded	Net Premium
Ordinary Life Insurance			
Permanent life	$ 7,631,472,142	$167,736,726	$ 7,463,735,416
Term	694,765,340	352,170,434	342,594,906
Variable Life	769,516,814	6,872,428	762,644,386
Individual Annuities			
Fixed deferred annuities	67,317,414		67,317,414
Variable deferred annuities	587,888,824		587,888,824
Payout annuities	21,813,127		21,813,127
Group Annuities	197,613,050		197,613,050
Group disability income	90,353,462	41,054,947	49,298,515
Individual disability income	588,670,255	10,501,189	578,169,066
	$10,649,410,428	$578,335,724	$10,071,074,704

III. MANAGEMENT AND CONTROL

Board of Trustees

NML's bylaws allow for a maximum of 30 members on the Board of Trustees. Currently the Board of Trustees consists of 24 members who are elected at the annual meeting of policyholders. The four-year terms of the trustees are staggered so that the policyholders elect approximately one fourth of the board each year. Members of the company's Board of Trustees may also be members of other boards in the holding company group. The trustees are compensated for their services as follows:

Trustees' Fee Schedule

	Annual Retainer	Attendance Fee
Trustees	$40,000	$1,500
Finance Committee Members	2,400	1,000
Other Committee Members		1,000
Outside Trustee Committee Chairs	5,000	1,250
Special Service by a Trustee		1,500
Examining Committee		2,000
Examining Committee Chair	3,000	2,000
Voting Inspectors		300

If committees meet on the same day as the Board of Trustees, an attendance fee is paid to members for each meeting. If a trustee substitutes as the chair of a committee, the chair's attendance fee is paid in place of the regular committee attendance fee. "Inside" Trustees do not receive board compensation

Currently, the Board of Trustees consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Edward E. Barr Fort Lee, NJ	Retired Chairman, Sun Chemical Corporation	2003
John M. Bremer Milwaukee, WI	Chief Operating Officer, Northwestern Mutual	2006
Peter W. Bruce Milwaukee, WI	Chief Insurance Officer, Northwestern Mutual	2004
Robert C. Buchanan Appleton, WI	President and CEO, Fox Valley Corporation	2003
George A. Dickerman Longmeadow, MA	Retired Chairman, Spalding Sports Worldwide	2004
Pierre S. du Pont Wilmington, DE	Director, Richards, Layton & Finger	2006

Board of Trustees (cont.)

Officers of the Company

Officers are elected at the board's annual meeting. Executive officers at and above the level of senior vice president at the time of this examination included the following:

Name	Office	2002 Compensation
Edward J. Zore	President and Chief Executive Officer	$3,644,637
Peter W. Bruce	Chief Insurance Officer	1,795,152
John M. Bremer	Chief Operating Officer	1,729,952
Mason G. Ross	Executive Vice President and Chief Investment Officer	1,545,877
William H. Beckley	Executive Vice President	1,194,732
John E. Schlifske	Senior Vice President	1,062,432
Bruce L. Miller	Executive Vice President	1,028,384
Deborah A. Beck	Executive Vice President	924,924
Frederic H. Sweet	Senior Vice President	880,161
Gary A. Poliner	Sr. Vice President and Chief Financial Officer	815,362
William C. Koenig	Sr. Vice President and Chief Actuary	720,199
Richard L. Hall	Senior Vice President	716,979
Charles D. Robinson	Senior Vice President	627,155
Leonard F. Stecklein	Senior Vice President	561,918
Barbara F. Piehler	Sr. Vice President and Chief Information Officer	376,835

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Executive Committee
Edward J. Zore, Chair
John M. Bremer
Peter W. Bruce
Robert C. Buchanan
James D. Ericson
David A. Erne
Stephen N. Graff
Daniel F. McKeithan, Jr.
Peter M. Sommerhauser
John J. Stollenwerk

Finance Committee
Edward J. Zore, Chair
Robert C. Buchanan
James D. Ericson
David A. Erne
Stephen N. Graff
Daniel F. McKeithan, Jr.
Peter M. Sommerhauser
John J. Stollenwerk

Audit Committee
Kathryn D. Wriston, Chair
Robert C. Buchanan
David A. Erne
Stephen N. Graff
Barry L. Williams

Agency and Marketing Committee
Sherwood H. Smith, Jr., Chair
George A. Dickerman
James D. Ericson
Barbara A. King
J. Thomas Lewis
John J. Stollenwerk
Edward J. Zore

Human Resources and Public Policy Committee
Peter M. Sommerhauser, Chair
Edward E. Barr
Pierre S. du Pont
Patricia Alberg Graham
Stephen F. Keller
Daniel F. McKeithan, Jr.

Operations and Technology Committee
John E. Steuri, Chair
J.E. Gallegos
James P. Hackett
H. Mason Sizemore
Harold B. Smith
Edward J. Zore

IV. AFFILIATED COMPANIES

NML is the ultimate parent of a holding company system. The organizational chart following this section depicts the relationships among selected significant affiliates in the group. A brief description of the significant subsidiaries of NML is given in the following paragraphs.

Northwestern Long Term Care Insurance Company (NLTC)

NLTC was organized in Illinois in 1953 as the Poulsen Insurance Company of America. For most of its history, it was known as the Standard of America Life Insurance Company. NML acquired the company in 1982. On October 10, 1997, NLTC redomesticated from Illinois to Wisconsin and the present name was adopted. Prior to August 1998, NLTC's insurance business consisted of paying benefits on supplementary contracts purchased by contract owners from NLTC prior to 1996.

In August 1998, NLTC began selling its first long-term care product, QuietCare. QuietCare reimburses the insured for long-term care services up to a specified daily limit, ranging from $50 to $300 per day. The policyholder can receive reimbursement for some or all of the costs of care received at home, at an adult day care center, at an assisted living facility, or at a nursing home. Benefits begin after the policyholder has accrued either 90 or 180 days (chosen at time of purchase) of qualifying expenses. The policyholder can elect to receive benefits for three years, six years, or for life. The policy includes a waiver of premium provision. The policy is guaranteed renewable, but if experience by rating class deviates from expectations, NLTC will have the right to increase premiums (subject to required states' approvals). It is available to individuals 18 to 79 years old. NLTC reinsured 80% of this business in order to limit its exposure to loss on any single insured and to recover a portion of benefits paid. QuietCare will no longer be issued after March, 2003.

An enhanced product, QuietCare RS, was introduced in March 2002 and includes dividend participation, alternate living facility reimbursement up to 100% of the Nursing Home daily benefit, and a Caregiver Training benefit. Certain features of the new contract were made available to existing policyowners with no increase in current premiums. Since the new participating feature was provided to existing policyowners, all in-force policies are now participating. The new product is not reinsured.

Pursuant to the introduction of QuietCare, NML and NLTC entered into two agreements, which are described below.

Effective January 1, 1998, NML and NLTC entered into a Product and General Service Agreement, which replaced a previous service agreement. Under the terms of the current agreement, NML agreed to contribute to NLTC the long-term care product developed by NML at an amount that reflects NML's actual development expense. NLTC reported this transaction as a capital contribution. NLTC then expensed the development costs, and nonadmitted the related software. No goodwill was carried as a result of the transaction. In addition to the contribution of the product, NML agreed to provide all requested services including legal, accounting, investment, marketing, and information technology services as necessary for NLTC's operation. Reimbursement to NML for these services is based on actual expenses incurred and an allocation of shared costs based on the number of employee hours of service provided to each entity. The agreement also provides that rather than direct reimbursement from NLTC for future services, NML may choose to have its capital investment in NLTC increased by the value of the services rendered. This option was exercised for start-up costs incurred prior to the product's introduction in August 1998. Beginning in September 1998, NLTC began reimbursing NML for administrative expenses. The above agreement was executed with the consent of the Office of the Commissioner of Insurance.

Effective April 29, 1998, NML and NLTC entered into a Capital Support Agreement and Guarantee of Benefits under which NML agrees to maintain the capital and surplus of NLTC at a level that is greater than the lesser of a) 30% of earned premium plus 5% of the value of total net reserves, or b) 150% of the NAIC risk-based capital requirements applicable to NLTC. NML also guarantees to the policyholders of NLTC the ability of NLTC to pay all policy benefits due on contracts of insurance sold by NLTC during the term of the agreement. The agreement terminates at the earlier of ten years from the effective date or at such time as NML has invested a total of $400 million in NLTC. The guarantee to policyholders of NLTC survives the termination of the agreement. This agreement was executed with the consent of the Office of the Commissioner of Insurance.

The 2002 statutory annual statement reported assets of $71,929,772, liabilities of $16,348,030, and policyholders' surplus of $55,581,742. Operations for 2002 produced a net loss of ($17,619,217). NLTC was examined concurrently with NML.

Frank Russell Company (Russell)

NML acquired the Frank Russell Company effective January 1, 1999 for a purchase price of approximately $955 million plus contingent consideration. This acquisition was accounted for using the statutory purchase method, adjusted for the charge-off of acquisition goodwill. Since the date of the acquisition, NML has charged-off directly from surplus approximately $882 million, representing the goodwill associated with the acquisition. NML received permission from the Office of Commissioner of Insurance for this statutory treatment, which is different than the NAIC Accounting Practices and Procedures Manual.

Russell, a global investment services firm, provides manager-of-manager investment products and services in more than 35 countries. Russell manages $70 billion in assets. Founded in 1936, Russell is headquartered in Tacoma, Washington, with additional offices in New York, Toronto, London, Paris, Singapore, Sydney, Auckland, and Tokyo.

As of December 31, 2002, the audited financial statements reported assets of $1,260,230,000, liabilities of $792,574,000, and shareholders equity of $467,656,000. In 2002, the company reported net income of $45,900,000. As noted above, due to the charge-off of acquisition goodwill, NML's carrying value for Russell is approximately a negative $480 million.

Baird Holding Company (BHC)

BHC is a majority-owned subsidiary of NML (89.5%). BHC was formed in 2001, as an intermediate holding company for its majority-owned subsidiary, Baird Financial Corporation (BFC) and BFC's majority-owned subsidiaries, principally Robert W. Baird & Co. Inc. (Baird), and Baird UK Limited.

Baird is a Midwest regional securities broker and dealer that has been in business over 75 years. Baird engages in a broad range of activities in the securities brokerage and investment banking business, including private client brokerage transactions, private equity and venture capital investing, market making and trading activities, investment advisory and money management services. Baird, NML, and NMIS have executed an agreement under which NML provides advertising and marketing services for Mason Street Funds.

As of December 31, 2002, the consolidated financial statements of BHC reported total assets of $857,602,000, liabilities of $602,746,000, and stockholder's equity of $254,856,000. Operations in 2002 resulted in net income of $12,010,000.

Northwestern Mutual Investment Services (NMIS)

NMIS is a wholly owned subsidiary of NML that performs several services for companies in the NML group. As a broker/dealer, NMIS selects, trains, and supervises the financial representatives of NML who sell variable annuities and variable life insurance, and the financial representatives of NMIS who sell mutual funds, stocks, bonds and other securities. NMIS also acts as co-depositor with NML for certain variable annuity accounts and provides administrative services to NML with regard to these accounts. NML pays a management and office services fee to NMIS based on expenses incurred by NMIS in performing these services. This amounted to $10.0 million in 2002. NMIS also received $124.2 million of commission revenue from NML in return for commission expense incurred by NMIS in the sales of NML's variable products.

NMIS serves as distributor for Mason Street Funds, Inc. (MSF). NMIS receives payment for these services through underwriter concessions, 12b-1 fees and CDSC fees. NMIS received $2.0 million of revenue for its MSF-related services in 2002.

NMIS is managed and operated by NMIS employees. NML employees perform services for NMIS, for which NML is reimbursed under a cost-sharing arrangement. The total amount paid to NML for these services was $26.8 million in 2002.

As of December 31, 2002, NMIS reported in its audited financial statements assets of $48,231,207, liabilities of $9,690,815, and member's equity of $38,540,392. Operations for 2002 resulted in a net loss of ($14,961,332). NMIS received a capital contribution in the amount of $25 million from NML in 2002.

Mason Street Funds, Inc.

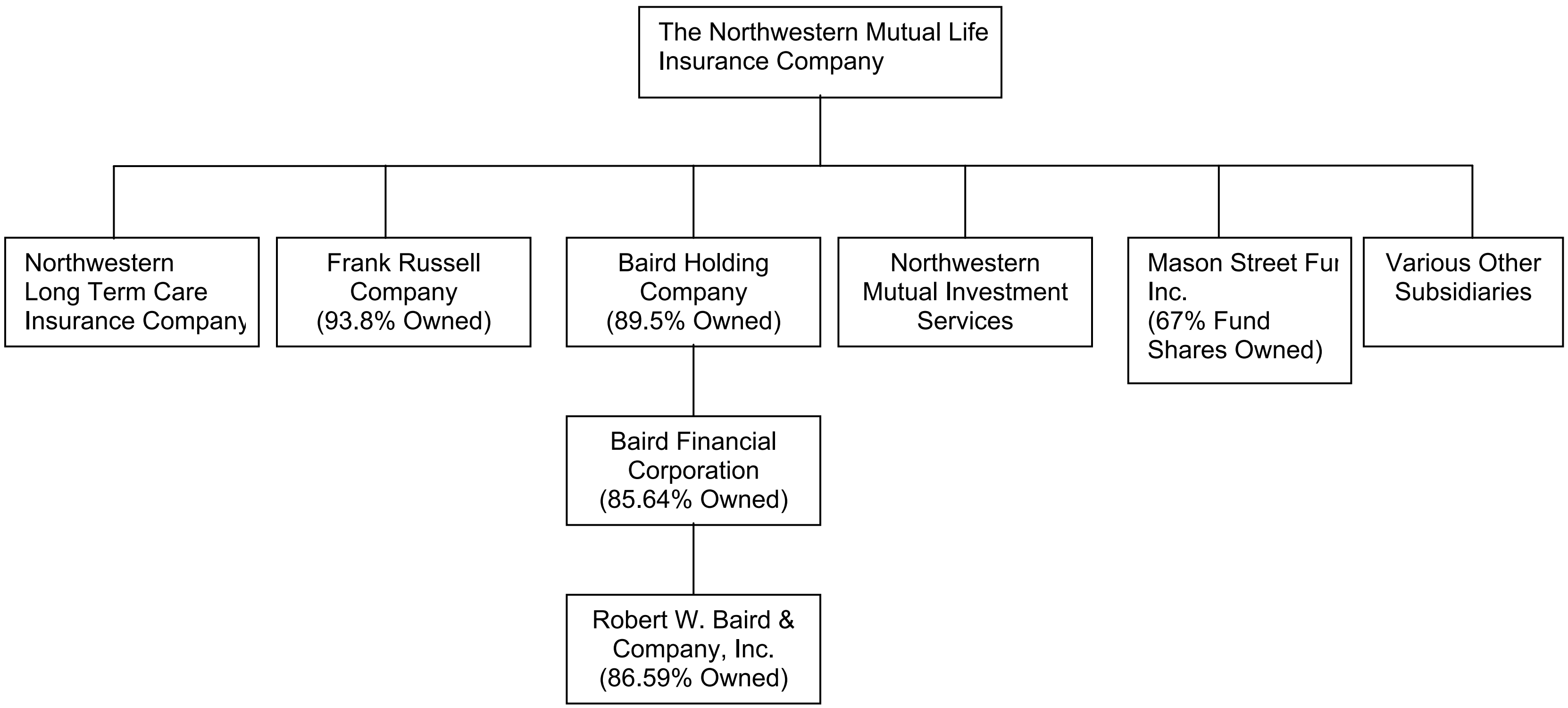
Mason Street Funds, Inc., was incorporated under the laws of Maryland on August 30, 1996, as an open-end investment company. This mutual fund group consists of eleven separate funds, each representing a separate class of capital stock. All funds commenced operations on March 31, 1997, except the two which commenced operations on July 12, 1999. NML established this group of mutual funds to provide an investment alternative for its policyholders and others. Mason Street Advisors, LLC is the investment advisor to the funds, and NMIS serves as distributor and broker/dealer. Each fund also pays the administrator, NML, a monthly fee at an annual rate of .10% plus cost for pricing securities. This administration fee is for services including recordkeeping, preparation of reports and fund accounting. As of March 31, 2003 the eleven funds held net assets of $1,162,354,377.

Other Affiliated Agreements

In addition to the agreements mentioned above, NML provided management and administrative services to NML Real Estate Holdings, LLC and NML Securities Holdings, LLC and other subsidiaries under the terms of individual service agreements. Fees collected by NML for the cost of allocable services performed for the subsidiaries totaled less than $70 million in 2002.

NML is also party to a consolidated federal tax agreement with certain affiliates, whereby it files its federal income tax on a consolidated basis. Under these agreements, separate tax liability calculations are performed for each of these affiliates together with all corporations directly or indirectly controlled by each affiliate which would otherwise be entitled or required to file consolidated federal income tax returns with that affiliate. In accordance with these calculations, each affiliate then either pays NML for any taxes so calculated or receives cash or credits from NML.

The Northwestern Mutual Life Insurance Company
Holding Company Chart
as of December 31, 2002



V. REINSURANCE

NML reinsures segments of its business to limit the amount of risk on an individual life, to provide a more competitive price for a broader range of policyholders, or to minimize the company's risk when entering a new line of business. The company cedes a relatively small amount of business to numerous unaffiliated companies. Ceded reinsurance premiums were less than 6% of direct premiums written in 2002. The company does not assume any reinsurance. The company's reinsurance portfolio at the time of the examination is described below. The contracts contained proper insolvency provisions.

Coinsurance of Term

The company currently coinsures, at 90%, four term insurance products to a pool of five reinsurers. NML determines the underwriting classification for this business, unless the term life coinsurance in force on the life exceeds $20 million or the total amount of insurance in force and applied for on the life in all companies exceeds $40 million. The policies are reinsured as long as they remain in force as term life, but the risk passes back to NML if the coverage is converted to a permanent life insurance plan. Reinsurance premiums are based on comprehensive schedules attached to the reinsurance agreements. NML receives a commission allowance for the first policy year of 100% of the reinsurance premium. NML's allowance for renewal years ranges from 30% to 50%, depending on the reinsurer, product, and underwriting class. Under this program in 2002, NML ceded approximately $49.5 million of gross first-year reinsurance premiums. The program included 964,000 policies and $301 billion of reinsurance in force at year-end 2002. The pool of reinsurers for new and in force business consists of:

Allianz Life Insurance Company of North America (Allianz)
American United Life Insurance Company
Business Men's Assurance Company (BMA)
Canada Life
Continental Assurance Company
General & Cologne Life Re (Cologne)
Lincoln National Life Insurance Company (Lincoln)
Munich American Reassurance Company
RGA Reinsurance Company (RGA)
Security Life of Denver Insurance Company (Security)
Swiss Re Life and Health America Inc
Transamerica

The percentage assumed by each participant varies depending on the specific product and series.

Automatic Reinsurance for Substandard Nonsmokers

Under this program, NML can offer a standard plus policy to nonsmoking applicants who meet the company's underwriting standards for substandard classes 1 to 5. The coverage is subject to a minimum of $50,000 and a maximum of $7.5 million of life insurance. The risk is 100% ceded automatically and the first $2 million of conditional receipt claims is split equally among the three reinsurers (except NML retains 50% of conditional receipt claims on lives it evaluates class 1). The reinsurance remains in force as long as the policy remains in force, even if it is on a term life policy later converted to permanent life coverage. The current participating reinsurers are Allianz, BMA, and RGA. This program resulted in $1.9 million of ceded first-year premiums in 2002. This program covered 85,000 policies and $20 billion of reinsurance in force at year-end 2002.

Automatic Reinsurance for Substandard Smokers

Under this program, NML can offer a class 2 policy providing $50,000 to $7.5 million of life insurance to smoking applicants who meet the company's underwriting standards for its smoker substandard classes 3 to 6. As with the program above, the risk is 100% ceded automatically and the first $2 million of conditional receipt claims is split evenly among three reinsurers. The current participating reinsurers are Allianz, AUL, and RGA. This coverage also continues for the lifetime of the underlying coverage. This program resulted in $213,000 of ceded first-year premiums in 2002. The program covered 6,000 policies and $1.1 billion of reinsurance in force at year-end 2002.

Facultative Substandard

Prepaid substandard applicants who do not qualify for one of the automatic programs and who meet specified face value or premium minimums are eligible for the facultative substandard reinsurance program. Under this program, underwriting papers are forwarded to several reinsurers who make competitive offers. The reinsurer offering the most favorable classification reinsures the entire contract; NML retains no mortality risk. This coverage continues for the lifetime of the reinsured coverage. This program involved $4.6 million of first-year reinsurance premiums, and $24 billion of reinsurance in force in 2002. Reinsurers currently participating under this program include Allianz, BMA, Cologne, and RGA.

Automatic and Facultative Excess Reinsurance

Effective October 1, 1998, the company established a retention limit on life insurance of $25 million for most ages. Allianz (15%), BMA (15%), Munich (22.5%), General & Cologne (22.5%), Gerling Global (10%) and SCOR (15%) provide automatic excess coverage up to $25 million (see the table below) for applicants rated in NML's best classifications (select, standard plus, standard, and smoker class 2). If approval of an application would result in either NML coverage on the life in excess of the approval authority or total insurance in all companies of more than the jumbo limit, the application must be submitted facultatively.

Issue Age	NML Retention	Automatic Reinsurance	NML Approval Authority	Jumbo Limit
0-60	$25 million	$25 million	$50 million	$50 million
61-70	12.5	12.5	25	50
71-75	5	10	15	50

Under the automatic and facultative excess programs, NML ceded $200,000 of first-year premiums in 2002. These programs represented about $2.0 billion of reinsurance in force as of December 31, 2002.

Automatic Reinsurance for Joint Substandard

The program provides automatic reinsurance of Joint CompLife or Variable Joint CompLife products with a minimum amount of $100,000 and maximum cumulative amount of $12 million for a pair of lives if either life is rated in any of five substandard nonsmoker or four defined smoker classes. (These are the same classes as the automatic reinsurance programs for nonsmokers and smokers, respectively.) The risks are shared equally by a pool of three reinsurers, AUL, Allianz, and RGA; Northwestern retains no mortality risk on these lives. This coverage also continues for the lifetime of the underlying coverage. Under this program, NML ceded $38,000 of first-year premiums in 2002. The program represented about $1.8 billion of reinsurance in force as of December 31, 2002.

Automatic Guaranteed Issue Reinsurance for Corporate Clients

A pool of three reinsurers provides automatic yearly renewable term (YRT) reinsurance of 90% of the mortality risk on Bank Owned (BOLI) and Corporate Owned (COLI) Life Insurance business. Current participating reinsurers include Munich, Swiss Re, and RGA. Amounts of insurance must be based on a formula benefit and are limited to an amount related to the number of lives in the group. This program allows the Company to write BOLI and COLI business to larger limits at more competitive premium rates than if retained. NML paid $1.4 million of first-year reinsurance premiums under this program in 2002. The program represented about $3.8 billion of reinsurance in force at year end 2002.

Group Disability Reinsurance

The company participates with Standard Insurance Company to offer both long-term and short-term disability coverages for employees of small businesses. Due to its group disability experience, Standard performs the product development, pricing, underwriting, and claims administration. The business is written on Northwestern paper, but Standard reinsures 60% of the risk. Northwestern recaptures the entire risk on any life who converts to individual disability income coverage upon leaving the employer. NML ceded $41.1 million of net (first-year and renewal) reinsurance premiums under this program in 2002. The program represented about $967 million of monthly benefit reinsurance in force at year end 2002.

Catastrophic Risk Reinsurance

The company participates with approximately 80 other companies in an individual life insurance catastrophe reinsurance pool. Coverage is provided whenever three or more lives insured by the same company die from a common catastrophe. The pool pays the total death benefit less (a) cash values, (b) amounts recoverable from commercial reinsurance, and (c) a fixed amount based on the insurer's individual life insurance in force. Each participating company shares in the claims against the pool according to a predetermined formula based on number of policies and average policy size. The company's share for the first half of 2003 is approximately 14%. Annual fees are determined on a sliding scale based on the company's in force amount. The fees range from $1,000 to $27,000.

VI. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported in the December 31, 2002, annual statement to the Commissioner of Insurance. Also included in this section are schedules which reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

The Northwestern Mutual Life Insurance Company
Assets
As of December 31, 2002

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$50,540,863,803	$ 0	$50,540,863,803
Stocks:			
Preferred stocks	810,614,112		810,614,112
Common stocks	4,136,195,898		4,136,195,898
Mortgage loans on real estate:			
First liens	15,512,041,402		15,512,041,402
Other than first liens	179,505,653		179,505,653
Real estate:			
Occupied by the company	123,699,572		123,699,572
Held for production of income	1,332,468,526		1,332,468,526
Held for sale	46,456,223		46,456,223
Policy loans	9,293,166,134	821,487	9,292,344,647
Premium notes	1,326	1,326	
Cash	249,659,179		249,659,179
Short-term investments	1,561,430,554		1,561,430,554
Other invested assets	4,111,359,812	5,380,912	4,105,978,900
Receivable for securities	9,374,012		9,374,012
Write-ins for invested assets:			
Insurance service account loans	6,644,454		6,644,454
Investment in process	39,430,094		39,430,094
Financial options and futures	651,538		651,538
Other	79,756,681		79,756,681
Reinsurance ceded:			
Amounts recoverable from reinsurers	38,777,866		38,777,866
Commissions and expense allowances due	12,167,070		12,167,070
Electronic data processing equipment and software	112,077,423	92,302,888	19,774,535
Federal and foreign income tax recoverable and interest thereon	1,887,508,169		1,887,508,169
Life insurance premiums and annuity considerations deferred and uncollected on in force business	1,214,225,014	7,923,835	1,206,301,179
Accident and health premiums due and unpaid	1,111,523	22,260	1,089,263
Investment income due and accrued	1,124,864,613	25,394,783	1,099,469,830
Receivable from parent, subsidiaries and affiliates	19,906,615		19,906,615
Amounts due from agents	90,628,185	90,628,185	
Other assets nonadmitted:			
Furniture and equipment	50,240,293	50,240,293	
Write-ins for other than invested assets:			
Amounts recoverable from state guaranty	2,136,601		2,136,601
Misc. accounts receivable	10,426,756	10,426,756	
Employees and agents trust	358,045,729		358,045,729
Others	82,294,787	81,565,177	729,610
From Separate Accounts Statement	10,245,589,730		10,245,589,730
Total Assets	$103,283,319,347	$364,707,902	$102,918,611,445

The Northwestern Mutual Life Insurance Company
Liabilities, Surplus, and Other Funds
As of December 31, 2002

Aggregate reserve for life policies and contracts		$68,755,386,794
Aggregate reserve for accident and health contracts		3,811,523,240
Liability for deposit-type contracts		1,741,004,447
Contract claims:		
Life		196,678,418
Accident and health		28,290,050
Policyholders' dividends and coupons due and unpaid		8,046,062
Provision for policyholders' dividends and coupons payable in following calendar year:		
Apportioned for payment to December 31, 2003		3,765,000,000
Premiums and annuity considerations received in advance		5,883,924
Contract liabilities not included elsewhere:		
Interest maintenance reserve		520,501,525
Commissions to agents due or accrued		35,007,896
General expenses due or accrued		97,619,761
Transfers to separate accounts due or accrued (net)		(211,770,455)
Taxes, licenses, and fees due or accrued, excluding federal income taxes		17,363,117
Federal and foreign income taxes		777,402,290
Unearned investment income		184,580,368
Amounts withheld or retained by company as agent or trustee		41,823,028
Remittances and items not allocated		348,554,996
Miscellaneous liabilities:		
Asset valuation reserve		1,267,587,874
Reinsurance in unauthorized companies		3,529,234
Payable to parent, subsidiaries and affiliates		29,355,670
Payable for securities		2,654,102,531
Write-ins for liabilities:		
Interest on policy and contract funds due and accrued		3,820,564
Deferred commissions		394,037,988
Liability for deferred compensation plans		447,935,880
Other		532,613,084
From Separate Accounts Statement		10,245,589,730
Total Liabilities		95,701,468,016
Write-ins for special surplus funds:		
Contingency reserve for separate accounts	$ 750,000	
Unassigned funds (surplus)	7,216,393,429	
Total Capital and Surplus		7,217,143,429
Total Liabilities, Capital and Surplus		$102,918,611,445

The Northwestern Mutual Life Insurance Company
Summary of Operations
For the Year 2002

Premiums and annuity considerations for life and accident and health contracts		$10,071,074,702
Considerations for supplementary contracts with life contingencies		25,878,741
Net investment income		5,447,208,770
Amortization of interest maintenance reserve		25,890,100
Commissions and expense allowances on reinsurance ceded		165,283,882
Miscellaneous income:		
Income from fees associated with investment management, administration, and contract guarantees from separate accounts		197,329,550
Charges and fees for deposit-type contracts		37,199
Write-ins for miscellaneous income:		
Sundry receipts and benefit plans		69,544,726
Total income items		16,002,247,670
Death benefits	$ 1,108,331,612	
Matured endowments	41,890,697	
Annuity benefits	168,548,627	
Disability benefits and benefits under accident and health contracts	358,722,510	
Surrender benefits and withdrawals for life contracts	2,028,088,325	
Interest and adjustments on contract or deposit-type contract funds	138,801,884	
Payments on supplementary contracts with life contingencies	57,225,271	
Increase in aggregate reserves for life and accident and health contracts	6,181,156,755	
Subtotal	10,082,765,681	
Commissions on premiums, annuity considerations, and deposit-type contract funds (direct business only)	685,537,897	
General insurance expenses	680,384,003	
Insurance taxes, licenses, and fees excluding federal income taxes	152,683,031	
Increase in loading on deferred and uncollected premiums	28,579,215	
Net transfers to or (from) Separate Accounts	242,282,790	
Total deductions		11,872,232,617
Net gain from operations before dividends to policyholders and federal income taxes		4,130,015,053
Dividends to policyholders		3,791,947,702
Net gain from operations after dividends to policyholders and before federal income taxes		338,067,351
Federal income taxes incurred (excluding tax on capital gains)		(441,746,912)
Net gain from operations after dividends to policyholders and federal income taxes and before realized capital gains or (losses)		779,814,263
Net realized capital gains or (losses) less capital gains tax		(604,223,060)
Net Income (Loss)		$ 175,591,203

The Northwestern Mutual Life Insurance Company
Cash Flow
As of December 31, 2002

Premiums and annuity considerations for life and accident and health contracts			$ 9,927,985,025
Charges and fees for deposit-type contracts			37,199
Considerations for supplementary contracts with life contingencies			25,878,741
Net investment income			5,245,488,346
Commissions and expense allowances on reinsurance ceded			164,381,618
Fees associated with investment management, administration, and contract guarantees from separate accounts			197,329,550
Write-ins for miscellaneous income:			
Sundry receipts, adjustments and benefit plans			69,544,726
Total			15,630,645,205
Death benefits	$1,117,733,527		
Matured endowments	41,890,697		
Annuity benefits	168,548,627		
Disability benefits and benefits under accident and health contracts	358,691,864		
Surrender benefits and withdrawals for life contracts	2,028,088,325		
Interest and adjustments on contract or deposit-type contract funds	137,371,412		
Payments on supplementary contracts with life contingencies	57,225,271		
Subtotal	3,909,549,723		
Commissions on premiums, annuity considerations, and deposit type contract funds	682,448,000		
General insurance expenses	691,503,542		
Insurance taxes, licenses and fees, excluding federal income taxes	151,960,200		
Net transfers to or (from) Separate Accounts	257,462,978		
Subtotal		$ 5,692,924,443	
Dividends paid to policyholders		3,677,722,983	
Federal income taxes (excluding tax on capital gains)		350,901,077	
Total deductions			9,721,548,503
Net cash from operations			5,909,096,702
Proceeds from investments sold, matured, or repaid:			
Bonds	60,850,303,812		
Stocks	1,779,959,922		
Mortgage loans	1,532,066,190		
Real estate	467,913,211		
Other invested assets	474,274,590		
Net gains or (losses) on short-term investments	(158,079)		
Miscellaneous proceeds	1,070,512,135		
Subtotal	66,174,871,781		
Less: Net tax on capital gains (losses)	(102,321,910)		
Total		66,277,193,691	

Less: Cost of investments acquired (long-term only):			
Bonds	67,378,484,192		
Stocks	2,035,876,240		
Mortgage loans	2,005,247,349		
Real estate	190,511,203		
Other invested assets	620,817,584		
Miscellaneous applications	127,256,759		
Total investments acquired		72,358,193,327	
Net increase (decrease) in policy loans and premium notes		264,416,320	
Net cash from investments			(6,345,415,956)
Cash provided from financing and miscellaneous sources:			
Deposits on deposit-type contract funds and other liabilities without life or disability contingencies	1,081,594,000		
Other cash provided	105,182,309		
Total		1,186,776,309	
Cash applied for financing and miscellaneous uses:			
Withdrawals on deposit-type contract funds and other liabilities without life or disability contingencies	832,902,151		
Other applications	119,638,363		
Total		952,540,514	
Net cash from financing and miscellaneous sources			234,235,795
Net change in cash and short-term investments			(202,083,459)
Reconciliation			
Cash and short-term investments, December 31, 2001			2,013,173,193
Cash and short-term investments, December 31, 2002			$ 1,811,089,734

The Northwestern Mutual Life Insurance Company
Compulsory and Security Surplus Calculation
December 31, 2002

Assets			$102,918,611,445
Less security surplus of insurance subsidiaries			3,064,016
Less liabilities			95,701,468,016
Adjusted surplus			$7,214,080,288
Annual premium:			
Individual life and health	$5,480,691,363		
Factor	15%		
Total		$822,103,704	
Group life and health	$ 91,647,391		
Factor	10%		
Total		9,164,739	
Greater of 7.5% of consideration or 2% of reserves for annuities and deposit administration funds		83,451,275	
Compulsory surplus (subject to a $2,000,000 minimum)		914,719,719	
Compulsory surplus excess or (deficit)			$ 6,299,360,569
Adjusted surplus			$7,214,080,288
Security surplus: (140% of compulsory surplus, factor reduced 1% for each $33 million in premium written in excess of $10 million with a minimum of 110%)			1,006,191,690
Security surplus excess or (deficit)			$6,207,888,598

The Northwestern Mutual Life Insurance Company
Reconciliation and Analysis of Surplus
For the Five-Year Period Ending December 31, 2002

The following schedule is a reconciliation of total surplus during the period under examination as reported by the company in its filed annual statements:

	1998	1999	2000	2001	2002
Capital and surplus, beginning of year	$4,100,631,694	$4,740,819,569	$5,069,022,421	$5,895,849,437	$6,891,802,763
Net income	808,886,407	1,336,641,199	1,828,752,725	661,558,173	175,591,203
Change in net unrealized capital gains or (losses)	(146,562,935)	212,684,454	(1,042,515,828)	(567,446,350)	(531,879,510)
Change in net deferred income tax				73,642,838	44,397,491
Change in non-admitted assets and related items	(2,858,038)	(2,216,972)	(21,879,075)	(115,878,210)	(104,344,122)
Change in liability for reinsurance in unauthorized companies	685,102	72,019	(1,414,948)	818,293	(2,827,759)
Change in reserve on account of change in valuation bases				(61,079,847)	
Change in asset valuation reserve	(19,962,661)	(377,002,038)	75,684,142	264,247,687	763,004,111
Cumulative effect of changes in accounting principles				749,334,742	
Charge-off of excess goodwill		(841,975,810)	(11,800,000)	(9,244,000)	(18,600,748)
Capital and surplus, end of year	$4,740,819,569	$5,069,022,421	$5,895,849,437	$6,891,802,763	$7,217,143,429

Despite realized and unrealized capital losses of approximately $1.1 billion and record anticipated dividends to policyholders of nearly $3.8 billion, surplus increased approximately $325 million in 2002.

The Northwestern Mutual Life Insurance Company
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2002

The following is a summary of NAIC Insurance Regulatory Information System (IRIS) results for the period under examination. There were no exceptional ratios.

	Ratio	1998	1999	2000	2001	2002
#1	Net change in capital & surplus	16.0%	7.0%	16.0%	17.0%	5.0%
#2	Gross change capital & surplus	16.0	7.0	16.0	17.0	5.0
#3	Net income to total income	6.0	9.0	11.0	4.0	1.0
#4	Comm and Exp to Prem and Deposits	Discontinued				
#5	Adequacy of investment income	197.0	189.0	196.0	187.0	169.0
#6	Non-admitted to admitted assets	0.0	0.0	0.0	0.0	0.0
#7	Total real estate & mortgage loans to cash & invested assets	23.0	24.0	23.0	23.0	22.0
#8	Total affl investments to capital & surplus	20.0	1.0	0.0	24.0	23.0
#9	Surplus relief	3.0	3.0	2.0	2.0	2.0
#10	Change in premium	10.0	4.0	7.0	6.0	8.0
#11	Change in product mix	0.0	0.0	0.0	0.0	0.3
#12	Change in asset mix	0.0	0.0	0.0	1.0	0.6
#13	Change in reserving ratio	3.0	(2.0)	(1.0)	1.0	3.0

Growth of Northwestern Mutual Life Insurance Company

Year End	Admitted Assets	Liabilities	Surplus
1997	$71,076,085,565	$66,975,453,871	$4,100,631,694
1998	77,989,750,906	73,248,931,338	4,740,819,568
1999	85,972,697,445	80,903,675,025	5,069,022,420
2000	92,111,866,461	86,216,017,024	5,895,849,437
2001	98,379,554,914	91,487,752,151	6,891,802,763
2002	102,918,611,445	95,701,468,016	7,217,143,429

Life Insurance In Force (in thousands)

Year	Gross Direct And Assumed	Ceded	Net
1998	$536,378,962	$221,956,693	$314,422,269
1999	583,426,108	249,424,841	334,001,267
2000	633,955,713	278,909,295	355,046,418
2001	691,012,520	317,427,217	373,585,303
2002	751,164,441	356,988,035	394,176,406

Accident and Health

Year	Net Premiums Earned	Net Losses Incurred	Commissions Incurred	Other Expenses Incurred	Combined Loss and Expense Ratio
1998	$508,687,092	$479,072,612	$66,812,269	$93,783,671	125.8%
1999	537,849,122	415,689,808	68,178,415	101,534,238	108.8
2000	565,216,883	526,327,090	67,751,451	113,836,525	125.3
2001	597,473,268	536,816,306	70,493,475	117,227,431	121.3
2002	625,913,184	537,541,484	69,953,441	119,271,043	116.1

As the above tables demonstrate, the company has exhibited a pattern of consistent growth with admitted assets and surplus increasing 45% and 76%, respectively during the period under examination. NML's life insurance in force, which currently exceeds $751 million, is comprised of approximately 3 million policyholders with traditionally low lapse rates contributing to the reported increases.

Reconciliation of Surplus per Examination

No adjustments were made to surplus as a result of the examination.

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were sixteen specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the company are as follows:

1. ISA Service Fees — It is recommended that the company include ISA service fees that are attributable to modal life insurance premiums in premium income for premium tax purposes in Wisconsin, and in any other state where such fees are taxable.

   Action — Compliance.

2. Invested Assets — It is recommended that the company amend its custodial agreements such that they contain provisions requiring:

   a) that the custodian is obligated to indemnify NML for any loss of securities occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction; and

   b) that in the event there is a loss of the securities for which the custodian is obligated to indemnify NML, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

   Action — Noncompliance, see comments in the summary of current examination results.

3. Invested Assets — It is recommended that the company establish procedures such that if the automated reconciliation of the custodial accounts fails, a manual reconciliation is performed.

   Action—Compliance.

4. Invested Assets — Furthermore, it is recommended that procedures be established to reconcile report totals, in addition to individual items, at periodic intervals (such as every 24 months) to reveal items that may go undetected by the current program.

   Action—Noncompliance, see comments in the summary of current examination results.

5. Invested Assets — It is recommended that the company comply with the filing requirements set forth in the Purposes and Procedures Manual of the NAIC Securities Valuation Office by filing the required documents within 120 days of the acquisition of a security.

   Action — Noncompliance, see comments in the summary of current examination results.

6. Bonds — It is recommended that in future annual statements, the company report the par value of foreign bonds in U. S. dollars.

   Action — Compliance.

7. Real Estate — It is recommended that in future annual statements, the company report in the market value column of Schedule A the most recent appraised value of real estate.

   Action — Compliance.

8. Policy Loans — It is recommended that the company improve internal recordkeeping procedures so that documentation of policy loan authorizations is maintained, pursuant to s. Ins. 6.80, Wis. Adm. Code.

   Action — Compliance.

9. Receivable for Securities — To avoid confusion with the preprinted line, it is recommended that the company use a different title than “Receivable for Securities” for the write-in asset representing items not collected within 15 days.

   Action — Compliance.

10. Aggregate Reserves for Life Policies and Contracts — It is again recommended that the company develop a set of reasonableness checks, such as average reserve factors over time, which can be used to detect unusual variations in reserve values, especially those produced by highly mechanized and summarized processes.

    Action — Compliance.

11. Aggregate Reserves for Accident and Health Policies — It is recommended that the company consider the need to perform cash flow testing (or additional sensitivity analysis) on its disabled life reserves in addition to claim run-off studies. If the company determines that no need exists, it should document the basis for that decision.

    Action—Compliance.

12. Aggregate Reserves for Accident and Health Policies — It is again recommended that the valuation summaries be expanded to provide a better audit trail so that actual tabular application of minimum standards can be more readily verified. In addition the company should regularly produce ratio tests of reserves on base policies and major ancillary benefits per unit of insurance in force so they can be monitored for reasonableness from year to year.

    Action—Compliance.

13. Provision for Policyholder Dividends Payable in Following Calendar Year — Pursuant to s. Ins 6.80, Wis. Adm. Code, it is recommended that the company establish a detailed dividend master file to provide support for this liability.

    Action — Compliance.

14. Commissions to Agents Due or Accrued — Pursuant to s. Ins 6.80, Wis. Adm. Code, it is recommended that the company establish such systems and procedures that are necessary to assure that the annual statement balance for this liability can be reconciled to detailed accrued commission data.

    Action — Compliance.

15. Remittances and Items Not Allocated — It is again recommended that accounts that do not meet the definition of Remittances and Items Not Allocated as stated in the NAIC Accounting Practices and Procedures Manual for Life and Accident and Health Insurance Companies be classified on appropriate lines in future annual statements.

    Action — Compliance.

16. Remittances and Items Not Allocated — It is recommended that the company establish procedures to periodically review suspense accounts and sublevel accounts to assure that balances over 120 days old are investigated and resolved.

    Action — Compliance.

Summary of Current Examination Results

Report of Executive Compensation

The State of Wisconsin requires each Wisconsin domiciled insurer to file a supplement to the annual statement entitled, “Report of Executive Compensation”, pursuant to ss. 601.42 and 611.63 (4), Wis. Stat. This report includes the total annual compensation paid to each director, the chief executive officer, and the four most highly compensated officers or employees other than the chief executive officer. In addition, the report requires disclosure of the compensation of all officers and employees whose compensation exceeds specified amounts. For an insurer of NML’s size, the compensation of each officer or employee whose annual compensation exceeds $200,000 must be disclosed.

The company failed to include certain unqualified compensation benefit amounts in the total compensation amount reported for certain executives. None of these omissions resulted in material understatement of reported compensation amounts. However, it is recommended that the company properly complete the “Report of Executive Compensation”, as required by ss. 601.42 and 611.63 (4), Wis. Stat.

Safekeeping Agreements

Many of the company’s securities are held by two banking and trust companies under the terms of two separate custodial agreements. The NAIC Financial Condition Examiners Handbook prescribes certain provisions which should be included in custodial agreements that indemnify the insurance company for lost or stolen securities, and require prompt replacement of lost securities. The previous examination noted that the terms of each of the agreements under which NML’s securities were held were either vague when compared to the NAIC’s required language or lacked the sufficient indemnification language as required. NML properly amended one of the agreements to contain the appropriate language. However, one agreement continued to lack the proper indemnification language. It is again recommended that the company amend its custodial agreements such that they contain provisions requiring:

a) that the custodian is obligated to indemnify NML for any loss of securities occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction; and

b) that in the event there is a loss of the securities for which the custodian is obligated to indemnify NML, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

Custodial Reconciliations

Following the end of each quarter, NML reconciles the company's investment system with the custodial statements through an automated process. The company's program compares information downloaded from each custodian with information from the general and separate accounts' inventories. Differences are listed on exception reports, which are then reviewed and reconciled manually. The previous examination recommended improvements to controls related to this reconciliation process. One recommendation required the company to establish procedures such that if the automated reconciliation of the custodial accounts fails, a manual reconciliation is performed. The other recommendation required the company to establish procedures to reconcile report totals, in addition to individual items, at periodic intervals (such as every 24 months) to reveal items that may go undetected by the current program. While NML established procedures to address concerns with a failure of the automated system, NML had yet to reconcile report totals to custodial accounts during the period under examination. It is again recommended that the company establish procedures to reconcile report totals, in addition to individual items, at periodic intervals (such as every 24 months) to reveal items that may go undetected by the current program.

During 2003, NML commenced implementation of a new investment system that in addition to other improvements is expected to more easily allow NML to reconcile report totals in compliance with this recommendation.

Invested Assets

NAIC designations are the specific alphanumeric symbols in use by the NAIC Securities and Valuation Office (SVO) to denote a category of credit quality for certain securities held by insurers. These NAIC designations range from 1 to 6, with NAIC 1 being assigned to obligations exhibiting the highest quality and NAIC 6 being assigned to obligations that are in or near default. In general, an insurance company is provided a rating after filing the security with the SVO. An insurance company may report a security with a "Z" suffix on its Schedule D for up to a year indicating that the current rating had been analytically determined by the company and will be submitted within 120 days to the SVO for valuation. Securities that are rated "Z" for more than one year default to an NAIC 6* designation and incur the most severe treatment under the NAIC Financial Conditions Framework.

The previous examination noted that NML was not in compliance with the filing requirements of the NAIC's Securities Valuation Office (SVO), as numerous securities had either not been filed within 120 days, as required, or had not been filed at all. In a letter dated August 28, 2002, the OCI again notified NML of various securities that appeared not to have been filed with the SVO. In a letter dated September 3, 2002, the company notified the OCI that, while the majority of securities in question had been filed with the SVO, certain of these securities had either been filed late or had yet to be filed.

The current examination again reviewed NML's compliance with the filing requirements of the SVO. Sample securities were selected from the "Examination Jumpstart" reports from the NAIC's database, which indicated securities owned by the company that did not appear on the SVO master file. The examination identified more than 15 instances where securities were not filed within 120 days as required, and had been reported as "Z" on the company's annual statement for more than one year. The company indicated that turnover within the investment reporting department contributed to this issue. It is again recommended that the company comply with the filing requirements set forth in the Purposes and Procedures Manual of the NAIC Securities Valuation Office by filing the required documents.

Private Placements

As of December 31, 2002, NML held approximately $15.8 billion in Private Placements. As part of its monitoring of private placements, NML requires issuers to file periodic financial statements in accordance with its private placement agreements. Financial statements are also required for filing purposes with the SVO. Currently, there is no formal process in place to obtain and track financial statements from issuers who have not provided this information in accordance with the covenants of the private placement agreements. As a result, monitoring of these investments and filing with the SVO are both hindered. It is recommended that the company establish procedures to ensure that financial statements are received for private placements in accordance with financial covenants to facilitate its review of financial position as well as filings with the SVO.

Provisionally Exempt Securities

As noted above, in general, an insurance company is provided a rating after filing the security with the SVO. However, securities that are rated and monitored by two or more acceptable Nationally Recognized Statistical Rating Organization (NRSRO), with no lower rating than the equivalent of an NAIC 2 Designation by any of the NRSROs, or securities that are rated and monitored by only one NRSRO, with a rating the equivalent of an NAIC 1 Designation, may be provisionally exempted (PE) from filing with the SVO. These securities are identified with the administrative symbol "PE" proceeding the NAIC designation.

Under the provisional exemption rules outlined by the Purposes and Procedures Manual of the NAIC Securities Valuation Office, an insurer initially determines if a security is eligible for exemption based on a three part test; a ratings test, an issuer test, and an optionality test. For each provisionally exempt security, the insurer is required to maintain a record supporting its decision, including details of the terms of the security, documents verifying the security's rating, and documents evidencing its continued monitoring of PE securities.

The examination revealed several instances wherein the company identified securities that were either not entitled to the provisionally exempt status or the provisionally exempt status had changed prior to year-end and the company had not properly updated the designation. The controls the company had established to address the provisionally exempt requirements were deemed to be insufficient to timely update changes to NRSRO ratings. Examples of inadequate controls included company personnel responsible for administering the provisionally exempt rules and reporting changes in ratings did not have direct access to rating changes made by the NRSRO's and had to request updates from other departments. This has lead to delays in reporting rating changes and in some cases, delay filing with the SVO, if securities lost its PE eligibility. It is recommended that the company develop and implement new written procedures related to PE securities that include maintaining a record supporting its decisions and evidencing its continued monitoring of the securities listed as PE to ensure the proper application of the provisionally exempt guidelines pursuant to the Purpose and Procedures Manual of the NAIC Securities Valuation Office.

As noted earlier, during 2003, NML commenced implementation of a new investment system that, in addition to other improvements, is expected to improve NML's controls/monitoring of PE securities. One of the features of the new investment system is it allows direct access to rating changes for personnel tracking the PE securities.

Securities Lending Program

The Company has entered into securities lending agreements whereby certain investment securities are loaned to third parties, primarily brokerage firms. All debt securities loaned are administered internally and the examination noted no concerns associated with this self-administered program.

NML has also entered into agreements with two banks to administer its equities securities lending programs and to act as custodian for the collateral received. One bank is utilized for its domestic equities lending program and the other for its foreign equities lending program. However, neither of the agreements contained the satisfactory indemnification language as specified in the NAIC Examiners Handbook. It is recommended that the company amend its agency agreements to include provisions requiring:

a) that the custodian is obligated to indemnify NML for any loss of securities/collateral in the custodian's custody occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction; and

b) that in the event that there is a loss of the securities for which the custodian is obligated to indemnify NML, the securities be promptly replaced or the value of the securities/collateral and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

According to Statements of Statutory Accounting Principles (SSAP), No. 18, paragraph 25, "In the event that foreign securities are loaned and the denomination of the currency of the collateral is other than the denomination of the currency of the loaned foreign securities, the amount of collateral shall be at least equal to 105 percent of the fair value of the loaned securities at that date. If at any time the fair value is less than 102 percent of the fair value of the loaned securities, the reporting entity must obtain additional collateral, the fair value of which together with the fair value of all collateral then held in connection with the transaction at least equals 105 percent of the fair value of the loaned securities." The agreement that related to NML's foreign securities lending program required 102% collateral instead of 105% as required. While the 105% standard has been followed in practice, it is recommended that the company amend its agency agreements to either include provisions requiring additional collateral requirements relating to collateral denominated in a different currency or include provisions that specify collateral must be denominated in the same currency as securities loaned.

NML had several controls in place to monitor the effectiveness of and compliance with agreements regarding the third parties administration of the equities lending programs. NML would notify the administrator of any apparent breaches with the agreements terms. However, NML did not periodically audit the adequacy of the collateral received by the administrator nor the timeliness of additional collateral received to address shortfalls. The examiners noted an instance where the market value of the collateral held was less than required by SSAP 18 and stipulated within the applicable agency agreement and additional collateral was not received in a timely manner. Failure to maintain sufficient collateral for the loaned securities would require NML to nonadmit the undercollateralized portion. The examination deemed the shortfall to be immaterial and thus proposed no adjustment. However, it is recommended that the company implement procedures to periodically, not less than annually, audit its securities lending programs administered by third parties to review for compliance with agreement provisions including but not limited to a review for compliance with collateral requirements.

Mortgage Loans **$15,691,547,055**

The balance for this account as of December 31, 2002, included a valuation allowance that had been established by NML for other than temporary impairments. According to SSAP, No. 37, paragraph 16, the use of a valuation account for impairments should be limited to temporary impairments and should be reported as an unrealized loss. For other than temporary impairments, NML should establish a new cost basis and recognize a realized loss for the mortgage loans in question. Neither reported surplus nor income was impacted by the error. However, it is recommended that in future annual statements, the company properly create a valuation allowance (a contra-asset) for the impairments deemed "temporary", or write down the mortgage loan (recognizing a realized loss and establishing a new cost basis) for impairments considered to be "other than temporary".

Other Long-Term Invested Assets **$4,105,978,900**

As of December 31, 2002, this account included NML's investments in oil and gas production, transportation equipment, joint ventures, partnerships, and limited liability company interests. The examination noted that NML reported actual cost equal to book/adjusted carrying value for many of these investments in Schedule BA of the annual statement. The NAIC's Annual Statement Instructions—Life, Accident and Health requires that companies report the actual cost as the cost of acquiring the asset, including broker's commission, incidental expense of effecting delivery, and all changes subsequent to acquisition, such as additions to or reductions in investments. The company indicated that this detailed information was not always readily accessible due to apparent system limitations and that it had determined in these cases to populate the actual cost column with the reported book/adjusted carrying value amounts. As of December 31, 2002, NML reported the actual cost equal to book/adjusted carrying value for over 50% of its Schedule BA assets. This reporting error makes it difficult for readers of the annual statement to determine the actual cost of reported investments. It is recommended that in future annual statements, the company report the actual cost column of Schedule BA in accordance with NAIC Annual Statement Instructions—Life, Accident and Health.

VIII. CONCLUSION

As of December 31, 2002, NML had total assets of $102,918,611,445, total liabilities of $95,701,468,016, and policyholders' surplus of $7,217,143,429. The company continues to grow steadily, and reported an increase to surplus during each year under examination. These traditionally positive results have allowed NML to continue to increase dividends to the reported $3.8 billion for 2002. This, coupled with NML's exclusive distribution system, has established high levels of brand loyalty exhibited by traditionally low lapse ratios. NML’s major product remains ordinary life insurance written on a participating basis.

The examination resulted in eleven recommendations, three of which were repeated from the previous examination. The remainder of recommendations related to safeguarding NML’s assets, filing securities with the SVO and financial reporting issues. No adjustments to surplus were made as a result of this examination. The company’s implementation of a new investment system is expected to assist the company in complying with several of the recommendations.

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 32 - Report of Executive Compensation—It is recommended that the company properly complete the "Report of Executive Compensation", as required by ss. 601.42 and 611.63 (4), Wis. Stat.

2. Page 32 - Safekeeping Agreements—It is again recommended that the company amend its custodial agreements such that they contain provisions requiring:

   a) that the custodian is obligated to indemnify NML for any loss of securities occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction; and

   b) that in the event there is a loss of the securities for which the custodian is obligated to indemnify NML, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

3. Page 33 - Custodial Reconciliations—It is again recommended that the company establish procedures to reconcile report totals, in addition to individual items, at periodic intervals (such as every 24 months) to reveal items that may go undetected by the current program.

4. Page 34 - Invested Assets—It is again recommended that the company comply with the filing requirements set forth in the Purposes and Procedures Manual of the NAIC Securities Valuation Office by filing the required documents.

5. Page 34 - Private Placements—It is recommended that the company establish procedures to ensure that financial statements are received for private placements in accordance with financial covenants to facilitate its review of financial position as well as filings with the SVO.

6. Page 35 - Provisionally Exempt Securities—It is recommended that the company develop and implement new written procedures related to PE securities that includes maintaining a record supporting its decisions and evidencing its continued monitoring of the securities listed as PE to ensure the proper application of the provisionally exempt guidelines pursuant to the Purpose and Procedures Manual of the NAIC Securities Valuation Office.

7. Page 36 - Security Lending Program—It is recommended that the company amend its agency agreements to include provisions requiring:

   a) that the custodian is obligated to indemnify NML for any loss of securities/collateral in the custodian's custody occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction; and

   b) that in the event that there is a loss of the securities for which the custodian is obligated to indemnify NML, the securities be promptly replaced or the value of the securities/collateral and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

8. Page 37 - Security Lending Program—It is recommended that the company amend its agency agreements to either include provisions requiring additional collateral requirements relating to collateral denominated in a different currency or include provisions that specify collateral must be denominated in the same currency as securities loaned.

9. Page 37 - Security Lending Program—it is recommended that the company implement procedures to periodically, not less than annually, audit its securities lending programs administered by third parties to review for compliance with agreement provisions including but not limited to a review for compliance with collateral requirements.

10. Page 38 - Mortgage Loans—It is recommended that in future annual statements, the company properly create a valuation allowance (a contra-asset) for the impairments deemed “temporary”, or write down the mortgage loan (recognizing a realized loss and establishing a new cost basis) for impairments considered to be “other than temporary”.

11. Page 38 - Other Long-Term Invested Assets—It is recommended that in future annual statements, the company report the actual cost column of Schedule BA in accordance with the NAIC Annual Statement Instructions—Life, Accident and Health.

X. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

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Sarah Haeft	Insurance Financial Examiner
Don Gasser	Insurance Financial Examiner
Bill Genne	Insurance Financial Examiner

Respectfully submitted,

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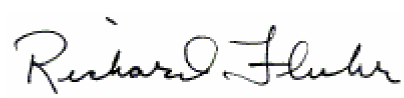
Insurance Financial Examiner - Senior



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